

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)	
Michigan Consolidated Gas Company)	Case No. U-15701-R
for a gas cost recovery reconciliation)	
proceeding for the 12 months ending)	
<u>March 31, 2010.</u>)	

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on July 14, 2011.

Exceptions, if any, must be filed with the Michigan Public Service Commission, P.O. Box 30221, 6545 Mercantile Way, Lansing, Michigan 48909, and served on all other parties of record on or before August 4, 2011, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before August 18, 2011. **The Commission has selected this case for participation in its Paperless Electronic Filings Program. No paper documents will be required to be filed in this case.**

At the expiration of the period for filing exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

MICHIGAN ADMINISTRATIVE HEARING
SYSTEM
For the Michigan Public Service Commission

Sharon L. Feldman
Administrative Law Judge

July 14, 2011
Lansing, Michigan

STATE OF MICHIGAN
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FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

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PROPOSAL FOR DECISION

I.

PROCEDURAL HISTORY

This Proposal for Decision addresses Michigan Consolidated Gas Company's June 29, 2010 filing for approval of its reconciliation of Gas Cost Recovery (GCR) costs and revenues for the GCR year ending March 31, 2010. The application identified a GCR overrecovery of approximately \$5.9 million, including interest through March 31, 2010. The company's application was accompanied by the prefiled testimony and exhibits of four witnesses: Barbara J. Goodwin, W. Bernard Kramer, Jennifer C. Schmidt, and Eric W. Clinton.

At the August 31, 2010 prehearing conference, the company and Staff appeared, and the following additional parties appeared and were granted intervention: the Attorney General; the Michigan Community Action Agency Association (MCAAA); and

the Residential Ratepayers Consortium (RRC).¹ Following the schedule established at the prehearing conference, on February 11, 2011, the Attorney General filed testimony and exhibits of Ralph E. Miller, the RRC filed testimony and exhibits of Frank J. Hollewa, and the MCAAA filed testimony and exhibits of William A. Peloquin. Also in accordance with the established schedule, Mich Con filed the rebuttal testimony of Ms. Schmidt and Mr. Clinton, along with a rebuttal exhibit on March 15, 2011, and motions to strike testimony of Mr. Hollewa and Mr. Peloquin on March 31, 2011; the RRC filed a response to the motion directed at Mr. Hollewa's testimony on April 7, 2011.

At the April 11, 2011 evidentiary hearing,² following rulings on the motions to strike, the testimony and exhibits of all witnesses except Mr. Clinton were bound into the record by agreement of the parties, without the need for the witnesses to appear.³ Mr. Clinton presented his testimony and exhibits and was subject to cross-examination.

Mich Con, the RRC, the Attorney General, and the MCAAA filed briefs on May 10 and reply briefs on May 24, 2011. Also, on May 20, 2011, Mich Con filed a motion to strike a portion of the brief filed by the MCAAA, asserting that the identified portion of the brief relied on evidence outside of the record. The MCAAA responded on June 27, 2011.⁴

¹ Administrative Law Judge Barbara A. Stump conducted the prehearing conference, held on August 31, 2010. Following her retirement, however, the case was transferred to Sharon L. Feldman.

² The originally-scheduled hearing date was adjusted with the concurrence of the parties, to accommodate the ALJ's schedule.

³ Some of the testimony was revised from versions initially prefiled.

⁴ In email to the ALJ, counsel for both Mich Con and the MCAAA indicated that they did not seek a hearing on the motion.

The evidentiary record is contained in 268 pages of transcribed testimony and 36 exhibits. The record and the positions of the parties are discussed in more detail below.

II.

OVERVIEW OF THE RECORD AND DISPUTED ISSUES

Mich Con's filing identified a net GCR overrecovery of \$3,958,773, plus interest of \$1,950,510, for a total overrecovery of \$5,909,289. The net overrecovery of approximately \$4 million is based on the GCR cost of gas sold of approximately \$959 million, GCR year adjusted (unbilled) revenues of approximately \$956 million, miscellaneous Gas Customer Choice (GCC) program fees and penalties totaling approximately \$1.2 million, and a rolled-in overrecovery of approximately \$5.4 million from the GCR year ending March 31, 2009.⁵

The company's direct case included testimony and exhibits presented by four witnesses, identified above, two of whom also provided rebuttal testimony. Ms. Goodwin, Principal Analyst in Gas Supply Planning for Mich Con, testified regarding Mich Con's actual operations during the GCR year compared to the GCR plan.⁶ The company's plan projected total gas supply of 171 Bcf, including approximately 145 Bcf for GCR customers and 26.2 Bcf for GCC customers, to meet a total sendout of 168 Bcf. In the GCR year, total gas supply of 168.7 Bcf was used to meet actual sendout of 164.2 Bcf, which reflected an 8.8 Bcf reduction in GCR sendout and a 5.1

⁵ See Exhibit A-18, page 2. The amount of the prior year's overrecovery is erroneously stated in several places in the record as \$8.4 million, including in Mich Con's application, in its initial brief, page 1 at note 1, and in Ms. Schmidt's testimony at 2 Tr 64.

⁶ Ms. Goodwin's testimony is found at 2 Tr 37-55.

Bcf increase in GCC sendout over the plan projection.⁷ Exhibits A-11, A-12, and A-15 compare actual supply sources with planned sources, by month and by operating season. Details on actual temperatures compared to normal weather are provided in Exhibit A-13 and details on the company's storage operations are provided in Exhibit A-14. Ms. Goodwin explained that colder-than-normal summer weather and warmer-than-normal winter weather affected the company's operations, as did customer migration to the GCC program, and other factors. She also testified to the impact of the Commission's March 5, 2009 order in Case No. U-15628 regarding native base gas.⁸ Exhibit A-16 shows the sources of supply and other statistics for the design peak day compared to the actual peak day for the GCR year.

Mr. Kramer, Regulatory Compliance Consultant for DTE Energy Corporate Services, testified regarding the regulatory actions Mich Con took during the GCR year to minimize interstate pipeline costs through participation in FERC proceedings, and presented Exhibit A-7 to summarize the company's efforts by pipeline and FERC docket.⁹ He also testified to Mich Con's new transportation contracts with ANR, not included in the GCR plan case, changes in Mich Con's transportation contracts with Trunkline and Panhandle, and costs above the plan forecast for TransCanada, due in part to increases in the tariff rate, exacerbated by increases in the cost of the Canadian dollar.

⁷ See Exhibit A-12, and Goodwin, 2 Tr 46.

⁸ See 2 Tr 42-44. The company reduced purchased volumes by 2 Bcf in the GCR year to accommodate the determination in Case No. U-15628 that 2 Bcf of base gas could serve as part of the company's colder-than-normal protection.

⁹ See 2 Tr 18-36.

Ms. Schmidt is a Principal Project Manager for DTE Energy Corporate Services LLC with a background in economics.¹⁰ Her direct testimony describes the calculation of the net overrecovery of approximately \$5.9 million including interest, and indicates that the calculations are consistent with the methodology used in past cases. Ms. Schmidt explained how certain volumes of gas are priced at the “jurisdictional rate”, including net exchange gas volumes from Mich Con’s affiliate MGAT, as well as company use, lost and unaccounted for gas, and gas in kind. Exhibit A-18 shows the gas volumes purchased and sold in the GCR year, the computation of the GCR cost of gas sold, adjustments to determine net recoverable costs, and the computation of the total GCR revenue. Exhibit A-19 contains supporting details on commodity, transportation and other costs as well as sales revenue, Exhibit A-20 shows the calculation of a storage cost adjustment, and Exhibit A-21 shows the interest calculation. Ms. Schmidt’s rebuttal testimony is discussed below.

Mr. Clinton is a Principal Analyst in the Gas Supply and Planning organization within Mich Con. He presented direct testimony addressing the natural gas purchasing decisions made by the company, including purchases of natural gas made at fixed prices under guidelines approved in prior GCR plan cases, as well as the term and spot market purchases Mich Con made to complete its supply requirements. Details of these transactions are provided in his Exhibits A-2 through A-7

Mr. Clinton testified that Mich Con’s filed plan included 76% fixed price purchases and 24% index-priced purchases, while its actual supply mix was 81% fixed price purchases, 19% index-priced purchases. His Exhibit A-2 identifies 109.8 Bcf of

¹⁰ Her direct testimony is at 2 Tr 56-66.

gas supplies purchased under fixed price contracts. He attributed the increased percentage of fixed price purchases to a number of factors outside Mich Con's control, including lower winter customer usage, higher GCC enrollment, a higher beginning gas storage balance from the prior GCR year, and the determination in Case No. U-15628 that 2 Bcf of convertible base gas could be used to meet part of the company's colder-than-normal protection requirement of 5 Bcf. As noted above, these factors were also discussed by Ms. Goodwin.

Mr. Clinton's Exhibit A-1 shows actual NYMEX prices during the GCR year averaged \$4.09 per Dth, in comparison to the plan case forecast of \$7.00 per Dth. Mr. Clinton acknowledged that the fixed price contract purchases delivered during the GCR year exceeded published index prices for the same period by \$460.4 million, or \$4.19 per Dth, but further testified that each time Mich Con contracted for the fixed price supply, the price fixed was the then-current market price for the delivery period.

Mr. Clinton also testified that Mich Con's gas purchases for the GCR period included 35.6 Bcf of index-priced gas at an average price of \$6.55 per Dth, but due to lower supply requirements and lower commodity prices, Mich Con actually purchased 25.7 Bcf of index-priced gas at an average price of \$3.63 per Dth.

Mr. Clinton testified to the company's total transportation costs, with details in Exhibits A-8 and A-9, and he testified regarding certain affiliate transactions, with details in Exhibit A-10. Mr. Clinton also testified on rebuttal, as discussed below.

Mr. Hollewa, of Energy Planning and Engineering Consultants, testified on behalf of the RRC.¹¹ Mr. Hollewa focused on the \$460 million difference Mr. Clinton identified between the cost of the company's fixed price supply and the NYMEX value of those supplies in the month of delivery. He presented several criticisms of the company's gas purchasing decisions, and in particular the company's fixed price contracts, contending that Mich Con had failed to make reasonable and prudent purchasing decisions by failing to exercise discretion in administering the fixed price purchasing guidelines established in prior cases, had exceeded the purchase limitations in those guidelines in key respects, and had further failed to obtain competitive pricing on certain purchases. He recommended disallowances totaling \$55.4 million. He presented Exhibits RRC-1 and RRC-3 in support of his testimony. The RRC also introduced additional Exhibits RRC-4 through RRC-8 in cross-examination of Mr. Clinton.

Mr. Miller, an independent consulting economist, testified on behalf of the Attorney General.¹² He also noted the \$460 million cost difference identified by Mr. Clinton, which he characterized as an "economic disaster" for the company and his customers, but did not recommend any disallowance of costs attributable to the company's decision-making under the fixed price purchase guidelines. Instead, he recommended that the company analyze the guidelines and its implementation of the guidelines to determine what factors contributed to the large cost difference.

Mr. Miller also recommended a \$3.3 million reduction to the pricing of gas supplies Mich Con obtained from its affiliate MGAT. Recognizing that the Commission ruled on this issue in Case Nos. U-16146 and U-15451-R, Mr. Miller testified that it was

¹¹ See 2 Tr 246-266.

¹² Mr. Miller's testimony is found at 2 Tr 72-89.

appropriate that company “purchases” of gas from MGAT be priced at Mich Con’s city-gate monthly index price rather than the jurisdictional rate used in the company’s filing in this case.

Mr. Peloquin, a CPA and independent consultant, testified on behalf of the MCAAA.¹³ He also recommended a reduction in Mich Con’s approved cost of gas for the GCR period attributable to the MGAT volumes, but calculated a slightly larger adjustment of \$3.5 million. Mr. Peloquin additionally addressed the potential he perceived for the company’s GCR costs to be influenced by affiliates of Mich Con. He identified numerous affiliates as listed in DTE Energy Company’s annual report, and explained that some regulatory tools are available to limit the impact of affiliates on a public utility, which he testified fall under the rubric of “ring fencing”. His Exhibit MCAAA-1 excerpts portions of DTE Energy Company’s Form 10-K filing to show affiliates of Mich Con; Exhibits MCAAA-2 to MCAAA-4 provide policy discussions from other forums of tools to address affiliate impacts on public utilities. His specific recommendations are discussed in more detail below.

Mr. Clinton and Ms. Schmidt testified in rebuttal to the testimony of Mr. Miller, and Mr. Hollewa.¹⁴ Mr. Clinton testified further regarding the company’s fixed price purchases, addressing the disallowances recommended by Mr. Hollewa. He contended that the company was reasonable and prudent in its purchasing decisions, that its purchases followed the fixed price purchase guidelines in place at the time of each transaction, and that it obtained the best market prices available at the time of each

¹³ Mr. Peloquin’s testimony is found at 2 Tr 91-109.

¹⁴ See Clinton, 2 Tr 139-172; Schmidt, 2 Tr 67-69.

purchase, including the best “Henry Hub” and basis prices for each of the transactions. He presented Exhibit A-22 in support of his testimony.

Responding explicitly to Mr. Miller’s testimony, Mr. Clinton disputed that the fixed price purchase program had been an economic failure, and further opined that because the company had new guidelines in place following the Commission’s decision in Case No. U-16146, no additional analysis of the fixed price purchase program should be required.

Ms. Schmidt’s rebuttal addressed only the MGAT pricing recommendations of Mr. Miller and Mr. Peloquin. She testified that the gas volumes had already been “purchased”, and that price adjustments were therefore foreclosed by Commission order.

In their briefs, the parties largely adopt the positions taken by their witnesses. Mich Con requests that the Commission approve its reconciliation as filed, make several proposed findings of fact, and reject the disallowances and other requests for relief advocated by the intervenors. The proposed findings of fact are the following:

FINDING OF FACT NO. 1: MichCon took all appropriate legal and regulatory actions to minimize the cost of gas.

FINDING OF FACT NO. 2: MichCon’s actual system operations for [the] April 2009 through March 2010 GCR year were reasonable and prudent.

FINDING OF FACT NO. 3: MichCon’s gas supply decisions for the April 2009 through March 2010 GCR reconciliation period were reasonable and prudent.

FINDING OF FACT NO. 4: MichCon has a total over-recovery including interest for the GCR period of \$5.9 million.

The intervenors dispute at least proposed findings numbered 3 and 4 above. The RRC advances three of the four disallowances recommended by Mr. Hollewa, totaling \$51 million. Two of these are based on claims that Mich Con exceeded purchase limits in the fixed price purchase guidelines, and the third is based on the claim that Mich Con failed to obtain the market basis adjustment in purchases to be delivered to the ANR Southwest receipt point. The RRC also proposes an additional disallowance, which it describes but does not quantify, to address Mr. Hollewa's testimony that the company failed to exercise appropriate discretion in implementing the fixed price purchase guidelines. The RRC withdraws the disallowance proposed in Mr. Hollewa's testimony based on his contention that Mich Con's imprudent purchasing practices led the company to pay more than the NYMEX high on many of the days it purchased gas. Instead, the RRC recommends bidding practice and bid documentation requirements for the company's purchases in future GCR periods. The Attorney General asks the Commission to adopt Mr. Miller's recommendations. The MCAAA asks the Commission to adopt Mr. Peloquin's recommendations.

Each of the disputed issues is discussed in more detail below. Section III addresses the fixed price purchases made for the GCR period; section IV addresses the MGAT purchases and the Commission's decision in Case No. U-15628; and section V addresses the MCAAA's remaining issues regarding affiliate transactions. Mich Con's motion to strike a portion of the MCAAA brief is also addressed in section V.

III.

FIXED PRICE PURCHASES

As discussed above, the RRC recommends several disallowances based on the company's fixed price purchases, and both the RRC and the Attorney General seek other remedies related to the fixed price purchases. Mich Con instead seeks a finding that its gas purchases were reasonable and prudent.

As background to understanding these disputes, section A reviews the history of these guidelines. The RRC's claim that Mich Con failed to exercise discretion in the timing of its fixed price purchases, and its proposed disallowance related solely to that failure, is discussed in section B below. The proposed disallowances arising from the RRC's claims that the company exceeded limits in the fixed price purchase guidelines are discussed in sections C and D. The company's basis and NYMEX price negotiations are discussed in section E, including a discussion of the RRC's recommendations for a disallowance related to the basis adjustment and for other Commission action with regard to the NYMEX price component. The Attorney General's recommendation that Mich Con undertake an analysis of its GCR plan is addressed in section F.

A. Background

For several years, Mich Con's GCR plans have included guidelines for the acquisition of gas supplies at fixed prices, referred to generally as "fixed price purchase" or "FPP" guidelines. The fixed price purchases at issue in this proceeding were made between December 27, 2006 and November 15, 2008. The parties agree that the

guidelines covering these fixed price purchases were adopted in Case Nos. U-14717, U-15042, and U-15451.¹⁵ Although the guidelines were amended in each case, essential elements remained unchanged. The stated objective of each set of guidelines applicable to purchases in this proceeding is: “To create a purchasing strategy that effectively manages the impact of natural gas market volatility while emphasizing the purchase of fixed-price forward contracts having prices in the range of historically low price levels.”

The fixed price purchase guidelines approved in each of these dockets provided for the acquisition of supply in part based on a comparison of current NYMEX price projections to benchmarks, referred to as “price triggers” or “buy signals”, derived from historical NYMEX data. The method for making fixed price purchases one to five years before the start of a GCR period is referred to in the guidelines as the “Quarterly Index Method”, or QIM. While the guidelines identify other methods for making purchasing decisions, the QIM was the basis for the company’s purchasing decisions at issue in this case.¹⁶

Under the QIM, historical NYMEX settlement data are analyzed each month; rolling 12-month averages are computed over a 3-year period, and evaluated separately so that the most recent 12 data points are ranked from highest to lowest, and the most

¹⁵ See Case No. U-14717 (August 22, 2006 order, Attachment 3 to Settlement Agreement); Case No. U-15042 (August 21, 2007 order, and Exhibit A-17); Case No. U-15451 (August 26, 2008 order, and Exhibit A-8). Although the guidelines were further amended in the plan case covering this GCR period, Case No. U-15701, the parties agree that those guidelines do not apply to the fixed price purchases made for this GCR period. See Case No. U-15701 (April 30, 2009 and November 12, 2009 orders).

¹⁶ See Clinton, 2 Tr 126.

recent 24 and 36 data points are similarly ranked.¹⁷ The QIM identifies “buy signals” or “price triggers” when current NYMEX price forecasts compare favorably to the historical data by falling at various levels below the 50-th percentile average price within any of the groupings. These levels are referred to as the “2nd Quartile”, the “1st Quartile” and “below the 1st Quartile”. The guidelines match the length of the purchases (1, 2 or 3-year purchases) to the period of historical data generating the “buy signal” (12, 24 or 36 months of data). The guidelines further specify purchase limitations when “buy signals” are reached, as percentages of the company’s expected total supply.

In challenging certain QIM purchases under the various versions of the guidelines, the RRC presented Exhibit RRC-1, which is a listing of Mich Con’s QIM purchases for this GCR period by date. The purchases shown in Exhibit RRC-1 are the same purchases shown in Mich Con’s Exhibit A-2, but unlike Mich Con’s Exhibit A-2, Exhibit RRC-1 facilitates a comparison of the QIM purchases with the guidelines in effect at the time the purchases were made. Exhibit A-2, on which Exhibit RRC-1 is modeled, also includes various deal “amendments”, minor changes in volume or receipt point not relevant to any issue in dispute in this proceeding.

Also, in discussing the company’s fixed price purchases, it is important to note that neither exhibit contains the total volumetric targets used by Mich Con in implementing the guidelines. Mr. Clinton testified that the company’s fixed price purchases of 109.8 Bcf represented 75% of the company’s planned total purchase requirements for the GCR period,¹⁸ approximately 145 Bcf as shown in Exhibit A-12.

¹⁷ The guidelines adopted in Case No. U-14717 also had 48 and 60-month averages, which were used to make purchases for four and five-year periods, but no such purchases are at issue in this reconciliation.

¹⁸ See 2 Tr 126.

He did not provide information indicating how those volumetric targets changed over the period of time in which the purchases were made.¹⁹ Mr. Hollewa used a total supply volume of 150 Bcf, based on the company's GCR plan for the year ending March 31, 2009, to determine the percent of its total expected supply the company purchased at each point in time.²⁰ While he noted that the company should have taken into consideration that fixed price purchases made in 2006 and 2007 were based on a higher planned supply, no party directly challenged Mich Con's assertion that it was not able to foresee the lower volumes actually required for the plan year.²¹

B. August/September 2008 purchases

The RRC takes issue with the company's gas purchasing, contending in part that Mich Con failed to exercise discretion in implementing the guidelines. Focusing on the purchasing decisions made on August 28 and 29, and September 2, 2008, under the guidelines approved in Case No. U-15451, Mr. Hollewa reviewed the volume of purchases and the speed with which they were made, to conclude that the company was not reasonable and prudent in implementing the guidelines.

Section 3.2 of the guidelines, addressing purchases based on the 12-month QIM, i.e. purchases for one year only based on a comparison of then-current NYMEX prices to the 12 most recent rolling historical annual averages, provides as follows:

A rolling 12-month NYMEX data period will be used to determine the quartile ranges and percent of total purchases applied to Year 1 of the GCR Period, as follows:

- a. 15% of Year 1 volume at 2nd Quartile price level[;]

¹⁹ See 2 Tr 227-228.

²⁰ See 2 Tr 251, 256.

²¹ See Clinton, 2 Tr 124-125.

b. 10% of Year 1 volume at 1st Quartile price level, or \$0.30 less than the actual price locked in under 3.2.a above[;]

c. 10% of the Year 1 volume below 1st Quartile price level, or \$0.30 less than the actual price locked-in under 3.2.b above.²²

Mr. Hollewa testified that using the 12-month QIM, Mich Con purchased 15% of the expected total supply for the GCR year in just two days, on August 28 and 29, 2008, as “2nd Quartile” purchases; another 10% on just one day as “1st Quartile” purchases, only four days later on September 2, 2008; and yet another 10% as “below 1st Quartile” purchases nine days later, on September 11, 2008. He further explained:

Therefore, 100% of the Quartile purchases permitted for Year 1 under the Guidelines (35%) were made on only four out of ten consecutive trading days. I strongly disagree that these accelerated purchases for Year 1 exhibited discretion or were made in a prudent manner. This is because the 2009-2010 annual strip averages ranged from \$12.278 on 7/03/08 to \$9.747 on the last trading day for July (a price decrease of \$2.531); from \$10.086 on 8/01/08 to \$9.343 on the last trading day for August (a price decrease of \$0.743); and from \$9.447 on 8/27/08 to \$8.526 on 9/11/08 (a price decrease of \$0.921). In my opinion, under the market conditions that existed at the time, it would have been more logical to start the FPP on 9/11/08 instead of completing all FPP for the 2009-2010 GCR Year, especially since prices were falling so drastically in the two prior months. The Company may claim that such a conclusion is “impermissible hindsight”, but a price drop of \$3.752 from \$12.278 on 7/03/08 to \$8.526 on 9/11/08 spanning a period of 10 weeks can accurately be characterized as “free-fall”. Waiting for the price to drop further or at least making FPP over a longer period of time would not only have been prudent, but would have been common sense with recognizing of a falling market under the circumstances that existed at that time.²³

Although Mr. Hollewa did not propose a specific disallowance to address these purchases, which he also characterized as “technically correct” under the QIM, the RRC in its initial brief recommends that the Commission disallow the portion of the NYMEX-based purchase price for the purchases made between August 28 and

²² Exhibit A-8 from Case No. U-15451, page 2.

²³ See 2 Tr 253-254.

September 11, 2008 that exceeded the September 11, 2008 NYMEX price of \$8.5331 per Dth.²⁴

Mich Con contends that the RRC's objection to the purchases constitutes impermissible hindsight. Mr. Clinton, one of two gas buyers for Mich Con responsible for making these purchases, identified seven steps that Mich Con follows to ensure that its purchases are reasonable and prudent:

During this GCR period, MichCon followed all of the steps that a reasonable and prudent purchaser of natural gas should generally consider prior to executing a purchase under MichCon's Commission approved FPP program which included:

- 1) Analyzing historical price data on a monthly basis to determine the price at which future purchases would be made at or below (also known as a "price trigger");
- 2) Continually monitoring current natural gas market prices compared to the historical price trigger to determine if a buy signal occurs;
- 3) Making a determination of the appropriate quantity or volume of natural gas to purchase (e.g. 5% of supply requirements) when a buy signal occurs and the desired future time period over which the gas would be delivered (i.e. the delivery period). This determination would take into consider first, supply that is already under contract, secondly, additional supply that is necessary to reliably operate the gas distribution system and serve customers, and thirdly, the economics or price associated with various geographical sources of supply (i.e. basis price) considering all applicable pipeline transportation costs to transport supply from the production region or market zone to the distribution system;
- 4) Contacting MichCon's credit organization to obtain an assessment of MichCon's suppliers' creditworthiness including available lines of credit;

²⁴ See RRC initial brief, pages 3-5. In referring to the NYMEX price Mich Con achieved on September 11, 2008, this PFD presumes the RRC intended to refer to the NYMEX price of \$8.53 shown in column 8, lines 26-30, rather than the NYMEX target of \$8.5331 shown in column 12. The RRC does not calculate the total disallowance based on this approach, but it would be approximately \$20 million, substituting \$8.5331 in column 8, lines 14-25 of Exhibit RRC-1 and subtracting the resulting total cost from the total shown on that exhibit.

- 5) Requesting offer prices from three or more creditworthy suppliers specifying the delivery period or term of supply, the purchase location, and the purchase volume;
- 6) Upon receipt of supplier offers, confirming that the purchase price is at or below the historical trigger price, and that the purchase price is within a range of reasonableness based on a comparison of the varying supplier offers, prior day price settlement information, electronic price quote systems, and electronic exchanges for a similar volume, delivery period, and geographic location considering that prices are changing constantly, and
- 7) Finally, taking all of the information gathered into consideration as a whole prior to executing the purchase.²⁵

Mr. Clinton disputed Mr. Hollewa's claim that the company did not make the August and September 2008 purchases in a prudent manner. He testified that the purchases were made in accordance with section 3.2 of the guidelines, quoted above, and cited the first sentence of paragraph 3.7 of the guidelines, which states: "New (or increased) purchase volumes may, but are not required, to be executed immediately upon a drop in futures prices into each Quartile Range."²⁶ He further responded:

[I]t is unreasonable and imprudent for any buyer such as MichCon to wait for the market to fall even further when a buy signal occurs, because it is impossible to predict or time when a market hits bottom. Mr. Hollewa's rationale is nothing more than speculative market timing and would subject MichCon to a disallowance risk as prices may rise and the buy signal may disappear, and not repeat itself in the future. If MichCon were to engage in the speculative market timing suggested by Mr. Hollewa by hoping that the market continues to fall, but instead prices end up rising, then MichCon would likely be criticized for not executing the fixed price purchase according the Commission approved FPP guidelines when the buy signal occurred.²⁷

²⁵ See 2 Tr 142-144.

²⁶ See 2 Tr 163.

²⁷ See 2 Tr 163-164.

While Mr. Clinton testified that there were no compelling circumstances indicating Mich Con should deviate from its plan,²⁸ he did not contradict Mr. Hollewa's subsequent testimony that the market was in "free-fall" at the time the purchases were made.

This PFD agrees with the RRC that the guidelines call for discretion in their administration. Paragraph 3.7, quoted in part by Mr. Clinton, states in full:

New (or increased) purchase volumes may, but are not required, to be executed immediately upon a drop in futures prices into each Quartile Range. *In all cases, however, the Company shall schedule the acquisition of fixed-price gas supply contracts in a prudent manner, taking into account the rate of change in market prices, price trends, or any other factors that in its discretion are deemed appropriate.* It is anticipated that Quartile Indices targets may not be fully achieved due to unanticipated gas market volatility.²⁹

The use of "may, but are not required to" in the first sentence calls for the exercise of discretion. The second sentence makes clear that Mich Con is at all times to make reasonable and prudent decisions, and to consider factors including rates of change in market prices and price trends prior to purchasing. Also, paragraph 9.5 states:

Notwithstanding the foregoing, any purchases under these guidelines may be suspended or modified at the Company's discretion if at any time unusual, unforeseen, or extreme market conditions occur. Such conditions shall include, but are not limited to, events of force majeure, hurricanes, national or natural disasters, extensive national pipeline disruptions, unprecedented or extreme price levels of price movements, etc. Such suspensions or modifications to these fixed price guidelines may include, but are not limited to, the deferral of locking-in winter fixed prices until November of the current GCR Period or the early start of the 21-day Moving Average method into the immediately preceding January, February, or March.³⁰

Consistent with his testimony quoted above, Mr. Clinton made clear that Mich Con did not consider whether the exercise of discretion was appropriate under

²⁸ See 2 Tr 128.

²⁹ Exhibit A-8 from Case No. U-15451, page 3, emphasis added.

³⁰ See Exhibit A-8 from Case No. U-15451, page 9.

either of these paragraphs. The seven steps he identified prior to purchasing do not include review of the rate of change in market prices or price trends. He testified on cross-examination that he believed it is speculative to consider price trends, and that Mich Con does not engage in speculation.³¹

This PFD thus finds that Mich Con did not establish that its decision to purchase over 25% of its total anticipated supply requirements on essentially three consecutive trading days³² was reasonable and prudent, or consistent with its obligation under paragraph 3.7 to schedule the acquisition of fixed price supplies in a prudent manner. That the guidelines permit the company to make such a large purchase at one time is not equivalent to requiring the company to do so. The company was required to exercise discretion, and Mr. Clinton's testimony made clear that the company declined to do so. Market volatility, as well as the declining price trends that had been occurring over the prior two months as described by Mr. Hollewa, should have led the company to spread out its purchases over a longer period of time.

Nonetheless, the disallowance proposed by the RRC in response to the company's failure to spread out its purchases in a reasonable and prudent manner is not supported on this record. Had Mich Con exercised discretion, it is not clear that as a reasonable and prudent purchaser, it would have timed its purchases to acquire gas supplies at the rate it obtained on September 11, 2008. In this regard, this PFD accepts Mich Con's contention that it cannot be expected to identify the bottom of the market. It is one thing to conclude that Mich Con was imprudent in committing over 25% of its total

³¹ See 2 Tr 229.

³² Mr. Clinton stated that more than a weekend intervened between purchases on August 29 and September 2, but this PFD notes that September 1, 2008 was Labor Day, at least a non-working day for Mich Con.

expected purchase costs for the GCR year to prices representative of the market on three consecutive trading days of a year characterized by volatile prices,³³ and it is another to presume Mich Con could have achieved a particular price had it employed a more reasonable purchasing strategy. Missing from this record is an analysis showing a range of results that would have been achieved, had Mich Con spread out its purchases over a greater period of time.

C. One-year purchases (12-month QIM)

The RRC argues that Mich Con exceeded the 35% limit on one-year purchases using the 12-month QIM method in making the purchases on lines 38-41 of Exhibit RRC-1. Under the guidelines approved in Case No. U-15451 applicable to these purchases, one-year purchases using the 12-month QIM are capped at 35% of the expected total supply. Mr. Hollewa identified purchases on lines 14-19, 20-25, 26-30 and 38-41 of Exhibit RRC-1 as one-year purchases, with a total volume of approximately 42.5%.

Mich Con acknowledges the 35% limit on such purchases, but argues that even though the purchases are shown on Exhibit A-2 and Exhibit RRC-1 as one-year purchases, they were instead purchases under the 24-month and 36-month QIM.

Exhibit RRC-4 shows the applicable QIM “price trigger” or target values relied on by the company in making purchases under the guidelines. A comparison of the values on page 3 of Exhibit RRC-4 with the “NYMEX target values” on lines 38-41 of Exhibit RRC-1 confirms that the company was using the NYMEX target values of \$8.316

³³The company’s purchases on lines 14-25 of Exhibit RRC-1 cost approximately \$300 million and are thus approximately 25% of the company’s total planned gas purchase cost of \$1,178,600,000. See Clinton, 2 Tr 123.

associated with the 24-month QIM at the 2nd Quartile and \$7.915 per Dth associated with the 36-month QIM at the 1st Quartile in making the purchases on those lines. That is, although the contracts on lines 38-41 appear to be one-year contracts that would have been made under the 12-month QIM, Mich Con actually made them using the 24-month and 36-month QIM targets. Although purchases under the 24-month and 36-month QIMs are expected to match the historical periods, the guidelines provide for “truncated” purchases over shorter time periods.³⁴

D. Three-year purchases (36-month QIM)

The RRC also challenges the purchases made on lines 8 through 10 and 31 through 33 of Exhibit RRC-1 as exceeding the limit on 3-year purchases. Mr. Hollewa testified that the company purchased 5% of its projected total supply requirements using a 36-month QIM price trigger at the 2nd Quartile as shown in lines 1-4 of Exhibit RRC-1, another 5% using a 36-month QIM at the 2nd Quartile, as shown in lines 8-10 of Exhibit RRC-1, and an additional 5% using a 36-month QIM also at the 2nd Quartile, as shown in lines 31-33 of Exhibit RRC-1. The RRC interprets the applicable guidelines to limit the 3-year 36-month QIM purchases at the trigger level of the 2nd Quartile to 5%.

Paragraph 3.4 of the guidelines from Case No. U-15451 states:

A rolling 36-month NYMEX data period will be used to determine the quartile ranges and percent of total purchases applied collectively for Year 1 through 3, as follows:

- a. 5% of Year 1 through 3 volume at 2nd Quartile price level[;]
- b. 5% of Year 1 through 3 volume at 1st Quartile price level, or \$0.70 less than the actual price locked-in under 3.4.a above[;]

³⁴ See Exhibit A-8 from Case No. U-15451, paragraph 3.6.

c. 5% of the Year 1 through 3 volume below 1st Quartile price level, or \$0.70 less than the actual price locked-in under 3.4.b above.³⁵

Mich Con, however, interprets the guidelines to provide for a “roll over” of these limits. Mich Con notes that the purchases in lines 1-4 were made in one GCR year, the purchases in lines 8-10 were made the following GCR year, and the purchases in lines 31-33 were made the GCR year after that. Paragraph 3.9 of the guidelines adopted in Case No. U-15451 does provide for a roll-over as follows:

On the first day after the close of the April NYMEX contract each year, the future GCR annual period that was designated the “Year 1” now becomes the “Current GCR Period,” and what was formerly designated the “Year 2” now becomes the “Year 1” and continuing in the same manner through “Year 4” that becomes “Year 3”.³⁶

Similar provisions are found in paragraph 4, page 3 of the guidelines approved in Case No. U-15042 and paragraph 4, page 3 of the guidelines approved in Case No. U-14717.

If any of these guidelines covered purchases made in consecutive GCR periods, the roll-over provisions identified would be applicable. Instead, the guidelines adopted in Case No. U-15042 were approved by the Commission on August 21, 2007, and therefore covered the purchases on lines 8-10 of Exhibit RRC-1; the guidelines adopted in Case No. U-15451 were approved by the Commission on August 26, 2008, and therefore covered the purchases on lines 31-33 of Exhibit RRC-1. Because one set of guidelines does not span more than one set of purchases, it is necessary to look separately at the guidelines in effect for each set.

³⁵ Exhibit A-8, Case No. U-15451, page 3.

³⁶ See Exhibit A-8, Case No. U-15451, pages 3-4.

Thus, for the 5% of supply volumes purchased for a three-year period under the 36-month QIM at the 2nd Quartile as shown on lines 8-10, the question is whether the limitations in paragraph 1 on page 2 of the guidelines approved in Case No. U-15042 permitted the purchase given the prior purchase on lines 1-4. And for the 5% of supply volumes purchased for a three-year period under the 36-month QIM at the 2nd Quartile as shown on lines 31-33, the question is whether the limitations in paragraph 3.4 of the guidelines approved in Case No. U-15451 and quoted above permitted the purchase, given the prior purchases. This PFD finds that although the guidelines do not speak directly to this point, the language of each applicable set of guidelines contemplated the additional purchases made by Mich Con, subject to the overall cap of 75% for purchases made under the Case No. U-15451 guidelines, and 45% for purchases made under the Case No. U-15042 guidelines.³⁷ For this reason, this PFD recommends rejection of the disallowance proposed by the RRC.

E. Negotiated Prices

The fixed price purchases Mich Con negotiated have two components. The NYMEX value representing the price of natural gas delivered to the Henry Hub corresponds directly to the QIM price triggers, which are NYMEX-based. Gas for delivery to other receipt points is traded based on an adjustment to the NYMEX value, positive or negative, referred to as the “basis adjustment.” These two components of the purchase prices for each Mich Con purchase for the GCR year under review are shown in columns 10 and 11 of Exhibit A-2, and columns 8 and 9 of Exhibit RRC-1.

³⁷ See Case No. U-15042 (Exhibit A-17, page 2, paragraph 1, lines 35-37), Case No. U-15451 (Exhibit A-8, paragraph 3.6).

Mr. Hollewa's recommendations regarding the NYMEX and basis prices negotiated by Mich Con stem from his concern that the company unreasonably and imprudently rushed to make purchases when price levels reached the QIM triggers. Mr. Hollewa testified that he did not believe that enough representative bids from multiple suppliers were obtained in such a short time frame:

I believe that too many purchases in too short a time period created imprudence in price discovery, negotiation and solicitation of sufficient competing bids. The purchase of 109,920,480 Dth at a cost of \$883,286,685 over just 15 days did not reflect prudent judgment and achieved very undesirable results.³⁸

Mr. Hollewa examined both components of the purchase prices and recommended partial disallowances of \$4.4 million for the NYMEX price component and \$2.6 million for the basis component. In its initial brief, the RRC withdrew the proposed disallowance related to the NYMEX price paid, but instead asks the Commission to require greater structure for and documentation of Mich Con's negotiations in future cases, before accepting the resulting costs.

Mich Con disputes Mr. Hollewa's conclusion regarding the reasonableness and prudence of its gas purchasing decisions. The company argues that it followed the steps a reasonable and prudent gas purchaser would follow, and cites Mr. Clinton's testimony as to the seven steps the company follows in negotiating with its suppliers. These steps are quoted in section B above. A key step the company focuses on is Mr. Clinton's testimony that the company solicits offers from at least three of its creditworthy suppliers identifying the delivery date, volume and receipt points: "Mr. Clinton not only testified that MichCon already solicits a minimum of 3 bids for every fixed price

³⁸ See 2 Tr 265; also see 2 Tr 262.

purchase, but that MichCon followed all of the steps that a reasonable and prudent purchaser of natural gas should generally consider.”³⁹ From this, the company argues that the prices it negotiated are within a “range of reasonableness” created by the proximity of supplier offer prices or actual purchase prices to each other.⁴⁰

A review of the record shows that the company has not substantiated its claim that it solicits at least three offers specifying a given volume, delivery period and location. Although Mr. Clinton’s rebuttal testimony clearly stated that the company solicits offer prices from at least three creditworthy suppliers specifying the delivery period, delivery point and volume,⁴¹ in a discovery response and on cross-examination Mr. Clinton distinguished an “offer” from an “indication”:

There are three types of prices most commonly used by MichCon’s buyers. There is an indicative price, an offer price, and a bid price. An offer price is the asking price at which the seller or supplier is willing to sell a product. A bid price is the price at which the buyer, MichCon, is willing to buy a product. An indicative price is neither an offer price nor a bid price but an indication as to the value at which the seller or supplier believes they may be able to sell a specific product.⁴²

He acknowledged that the company does not necessarily solicit three “offers”.

Q: Now in your previous answer you said the Company seeks three or more indications from suppliers. Is that correct?

A: That is correct.

Q: Does the Company seek three or more offers from suppliers?

³⁹ See Mich Con reply brief at 25, citing Clinton, 2 Tr 143-144.

⁴⁰ See Mich Con reply brief, page 23; see also Clinton, 2 Tr 152-153, 156, 157.

⁴¹ See, e.g., 2 Tr 157: “[I]t is MichCon’s practice to request offer prices from three or more creditworthy suppliers specifying the delivery period or term of supply, the purchase location, and the purchase volume. See also 2 Tr 143, 2 Tr 152, 156 (“Another proven method of price discovery that is of most importance to MichCon is the proximity of suppliers’ offers to one another within a range of reasonableness, as these are the reliable creditworthy counterparties with whom MichCon has the ability to transact.”)

⁴² See 2 Tr 191; see also Exhibit RRC-7.

A: Not necessarily.⁴³

Even treating an “indication” as an “offer”,⁴⁴ Mich Con has not established that it solicits three indications for each purchase. Exhibit RRC-5 shows the terms of each purchase or “deal”, as well as the available documentation on the “indications” Mich Con received.⁴⁵ A review of this exhibit shows there are only 44 indications documented for the company’s 41 fixed price purchases, or an average of one per purchase. For many of the deals shown, Mich Con purchased from only one or two suppliers at a given receipt point, with no “indications” reflected. See, for example, the deals at lines 1-4, 7, 11-15, 43-44, 61 and 75. While Mr. Clinton testified that the absence of additional indications on this exhibit does not mean no additional indications were solicited, he also made clear he couldn’t supply any additional information regarding the history of negotiations beyond what is contained in Exhibit RRC-5.⁴⁶

In essence, the company relies on the existence of its deals as sufficient justification for the reasonableness of the deals. Mr. Clinton’s testified:

MichCon is seeking to obtain the lowest possible price when it purchases natural gas whereas the supplier is seeking to obtain the highest possible price. *The fact that a transaction occurred between two willing counterparties indicates the current market price.*⁴⁷

⁴³ See 2 Tr 209-210. Notwithstanding Mr. Clinton’s clarification, Mich Con’s reply brief argues that the company solicits at least three “verbal offers”. See Mich Con reply brief at 23.

⁴⁴ The key difference between the “indication” and the “offer” seems to be that the indication cannot simply be accepted by Mich Con to make a deal. For example, the deal on line 29 of Exhibit RRC-5 with supplier E was at a price above the indication on line 31 from the same supplier.

⁴⁵ See 2 Tr 210: “What is shown on here are the actual deals and the indications that were received.”

⁴⁶ See 2 Tr 193-196.

⁴⁷ See 2 Tr 157-158 (emphasis added). Also see 2 Tr 151-153, 156.

As noted above, Mich Con also relies on the similarity of purchase prices on the same date to show these prices were within the range of reasonableness.⁴⁸ But because the company has not established that its deals were negotiated through competitive bidding, it has not substantiated its claim that multiple purchases made on the same day at similar prices are therefore within a “range of reasonableness”.

Similarly, Mr. Clinton also contended that the suppliers each know that Mich Con will choose the lowest price among competing offers, and thus will provide Mich Con with their best price.⁴⁹ But the record does not establish that the suppliers each provide Mich Con with their lowest price. The only evidence to this effect comes from Mr. Clinton’s testimony, which is not persuasive without the safeguards of competitive bidding. The company’s deals were negotiated with only 10 suppliers, although indications were solicited from a total of 13 suppliers.⁵⁰ Mr. Clinton acknowledged that each supplier is seeking the highest possible price. Additionally, Mr. Clinton did not consider in negotiations whether the suppliers he was dealing with would be well aware of Mich Con’s “price triggers” or “buy signals”, calling such a consideration “speculative.”⁵¹ The existence of the multiple deals at different prices on the same date, for the same term and receipt point, without documentation of offers or “indications” rejected, also contradicts the company’s claim to have selected the lowest price among competing offers or “indications”.

⁴⁸ See Mich Con reply brief, page 23 (“The fact is that MichCon executed at least two purchases and as many as four, with different counterparties on each day, which clearly demonstrated a range of reasonableness as the price at which market participants were willing to sell.”)

⁴⁹ See 2 Tr 213, 214.

⁵⁰ The suppliers are identified by letter designation on Exhibit RRC-5.

⁵¹ See 2 Tr 201.

This PFD thus finds that Mich Con failed to establish it followed reasonable and prudent purchasing practices in purchasing natural gas for the GCR period. It is thus appropriate to evaluate the proposed disallowances and other recommendations of the RRC.

1. BASIS component

The RRC contends that one aspect of Mich Con's imprudent gas purchasing practices was that the company did not properly consider the basis adjustment. Mr. Hollewa compared the basis adjustment Mich Con obtained on ANR Southwest (ANR SW) and on Panhandle Eastern Pipeline (PEPL) to the basis adjustments obtained by two other utilities. He testified:

I examined the Basis column for reasonableness based on the results achieved by other Michigan gas utilities. MichCon is the only one to make two and three year FPP on a single day. That precluded my examination of those 20 purchases.

Also, the only common pipelines with MichCon for at least two out of the other three gas utilities involved PEPL and ANR SW. The Basis adjustment achieved by MichCon for PEPL was comparable to two others. However, the Basis adjustment achieved by MichCon for ANR SW was less than the (\$0.815) achieved by SEMCO Energy Gas company and Michigan Gas Utilities Corporation.

Mich Con made 8 annual purchases (4/1/09 – 3/31/10) on ANR SW with a weighted average Basis of (\$0.697) involving 60,000 Dth per day. Therefore, I am recommending a disallowance of \$2,584,200.⁵²

He further testified that 8 out of the 17 purchases Mich Con made in just four trading days in late August and early September, 2008 were purchases on ANR SW: "I

⁵² See 2 Tr 262.

do not believe enough representative bids from multiple suppliers were obtained in such a short period.”⁵³

In addition to maintaining that it did follow reasonable and prudent purchasing practices, Mich Con argues that Mr. Hollewa’s recommended disallowance is unsupported. Mich Con cites Mr. Clinton’s testimony:

Mr. Hollewa’s comparison is incorrect and inappropriate as he does not provide the facts necessary for this type of comparison such as the delivery period, purchase volume, purchase date and time of day for the other utilities. Further, such an analysis is both incorrect and inappropriate, as these utilities have different distribution systems, different points of interconnection to interstate gas supply, and thus they manage their gas supply portfolios differently.⁵⁴

Mich Con also challenges Mr. Hollewa’s testimony based on the rules of evidence, arguing that Mr. Hollewa’s opinion is “legally deficient” under MRE 703, because Mr. Hollewa did not present evidence of the basis adjustments bargained for by SEMCO and MGU on this record.⁵⁵

In its briefs, the RRC emphasizes Mich Con’s failure to follow reasonable and prudent purchasing practices, but does not address Mich Con’s challenge to the comparability of SEMCO and MGU data.

For the reasons stated above, this PFD concluded that Mich Con failed to establish that it followed reasonable and prudent gas purchasing practices. Nonetheless, this PFD does not recommend a disallowance based on the basis price differential identified by the RRC. The mere difference in the average basis price paid by Mich Con on the one hand and SEMCO and MGU on the other does not establish

⁵³ See 2 Tr 262.

⁵⁴ See 2 Tr 150-151.

⁵⁵ See Mich Con reply brief, page 22 at n17.

that had Mich Con's purchasing practices been reasonable and prudent, it could likely have negotiated the same basis price. There is no information on this record as to how the market prices of the basis adjustments varied over time, or as to any similarity in the timing of purchases made by Mich Con and the other two utilities.

2. NYMEX price component

Mr. Hollewa compared the NYMEX price component on the date of each agreement to the published NYMEX high for that date reported in *Gas Daily*, and determined that in 24 out of 41 transactions, the company purchased gas using a NYMEX price that was above the reported high, and in 7 of the remaining 17 transactions, the company's NYMEX purchase price was above the published closing price for the day, although below the high.⁵⁶ Mr. Hollewa was not able to review the remaining 10 transactions because they were for a three-year period and adequate data was not available.

In rebuttal testimony, Mr. Clinton testified that the *Gas Daily* published high price applied only to NYMEX trades taking place during the pit trading sessions between 9:00 a.m. and 2:30 p.m. weekdays, while NYMEX is traded electronically from 6:00 p.m. to 5:15 p.m. Sunday through Friday.⁵⁷ Mich Con purchases took place between 8:00 a.m. and 5:00 p.m. weekdays, with suppliers known to Mich Con.⁵⁸ While Mich Con does not trade either in the pit session or in the electronic market, Mr. Clinton presented Exhibit A-22 to show that using reported highs for the much longer electronic trading period, the NYMEX price Mich Con paid in the 24 transactions identified by Mr.

⁵⁶ See 2 Tr 263-264.

⁵⁷ See 2 Tr 155, 225-226.

⁵⁸ See 2 Tr 224, and Exhibit RRC-8.

Hollewa were below the NYMEX high.⁵⁹ Had Mich Con paid the NYMEX high price as measured by the electronic trading period for each of the 24 transactions identified by Mr. Hollewa, Mich Con would have paid an additional \$5.2 million.

In its initial brief, while withdrawing Mr. Hollewa's proposed adjustment based on the high prices published in *Gas Daily*, the RRC maintains that Mich Con should be required to provide some support to show that its NYMEX purchases are made at reasonable prices. Since Mich Con does not make fixed price purchases around the clock, the RRC urges that the Commission require the company in future cases to provide data reporting the NYMEX "high" applicable to the hours of each day in which it makes fixed price purchases. It also argues that Mich Con should solicit at least 3-5 bids for every fixed price purchase and it should provide documentation of those bids and their results in future GCR reconciliation cases.

Turning first to the bid requirements and bid documentation requested, this PFD finds that the general concerns the RRC raises over Mich Con's purchasing practices are quite significant. As discussed above, although Mich Con recites that reasonable and prudent purchasing practices include soliciting three or more offers, Mich Con has not shown that it follows this practice. In part, it appears that the company does not keep adequate information to substantiate its practices. In part, the company appears to rely on informal and incomplete "indications" to establish a "range of reasonableness" for prices. Mich Con also has not presented alternative documentation, for example NYMEX trade data, to show that the prices it negotiated are objectively reasonable.

⁵⁹ See 2 Tr 159.

Mr. Clinton testified regarding the lack of bid documentation, indicating that the company's GCR plan does not require that documentation be kept.⁶⁰ In its reply brief, Mich Con cites the following testimony to support its claim that documentation is not practical:

[A]n illustrative example that would help is Mich Con will send out letters in an e-mail to a group of suppliers that we know are active at a specific receipt point. That will indicate the term that we're looking for, the delivery period, the volume, it will indicate which receipt point we're looking at, and we will tell them that we're looking for an indication. They're going to provide their best indication as to where they believe they can sell the gas at.

Now from there we're going to look at the indications, myself, the other buyer. If there is – we may escalate it to a manager, but it is a discussion that occurs as to where we believe the market is for a specific product. Then we're going probably, we're calling back the person that we view has the lowest price and we're negotiating a price there. That price may be their offer price, it may be MichCon doesn't like their offer price, we correspondingly place a bid and they say that the minute you place a bid the deal is done. Then they took MichCon's bid. I mean it's a very fluid process, and I hope that explains how this works.⁶¹

While Mich Con cites Mr. Clinton's testimony as quoted above to support its claim that "offers" cannot be documented due to the fluidity of the process, this claim is at odds with Mr. Clinton's acknowledgement that the company does not necessarily solicit three verbal offers, but may solicit only one, and with his testimony that the indications are typically done through email letters. Moreover, Mr. Clinton's testimony at the cited passage does not establish that greater documentation of "verbal offers" is not possible, only that no such documentation is currently available. As Mr. Hollewa pointed out, the company entered into only 41 purchase agreements entered into on 15 days over three GCR years to supply approximately 109.8 Bcf of gas for the GCR

⁶⁰ See 2 Tr 193-194.

⁶¹ See 2 Tr 213-214.

year under review in this case. With two people assigned to this task, it is reasonable and appropriate for the Commission to expect better documentation.

Thus, recognizing that this is a GCR reconciliation rather than a plan proceeding, this PFD recommends that the Commission provide at least strong cautions to Mich Con regarding its purchasing practices and its documentation of those practices. The RRC requests that the Commission require Mich Con to solicit bids from 3-5 suppliers for future fixed price purchases. This PFD instead recommends that the Commission caution Mich Con that in future cases, should Mich Con rely on competitive bidding to establish the reasonableness of its contract prices, Mich Con will be required to establish that it solicited and received offers from a reasonable number of suppliers, and that it made a reasonable selection from among those offers. Moreover, the Commission should caution Mich Con that for any plan, the company remains obligated to support the reasonableness and prudence of its gas supply decisions, including any appropriate documentation. Mich Con cannot rely on the absence of documentation requirements in a GCR plan as justification for the absence of documentation in a reconciliation.

Turning to the RRC's request regarding NYMEX price information, the RRC seeks a requirement that Mich Con provide NYMEX market data contemporaneous to its purchases, to verify the reasonableness of the purchase prices. Consistent with the discussion above, Mich Con should expect to provide the parties and the Commission with documentation to support any claim it makes that it relied on external market data to verify the reasonableness of the prices it paid. Nonetheless, on this record, it is not clear that the specific NYMEX market data the RRC seeks, limited to the hours of Mich

Con's actual purchasing, is available. Thus, this PFD recommends that the Commission caution Mich Con that to the extent it relies on NYMEX market data to support the reasonableness of its purchases, it must be prepared to present the data to the Commission and to the parties.

F. Further analysis of fixed pricing purchasing

As noted above, the cost of the company's fixed price purchases for this GCR period were \$460 million more than the NYMEX cost of gas at the time of delivery. Consistent with Mr. Miller's testimony, the Attorney General urges that the Commission require Mich Con to provide an analysis of factors leading it to incur gas commodity costs significantly in excess of actual market prices at the time of delivery. Mr. Miller testified:

If adherence to the GCR plan causes MichCon to incur \$460 million of extra costs, it is – or should be – incumbent upon MichCon to examine its fixed price purchases to find out how and why the GCR plan caused this enormous economic loss to its customers and to the economy of its service area and the entire state of Michigan. This analysis is urgently needed to guide the development of future GCR plans, so that economic losses like this one can be avoided or at least reduced in future years.⁶²

In addition to an analysis to guide future GCR plans, he called for an analysis in future GCR reconciliation proceedings in which there is a large difference between the company's contract costs and market costs at the time of delivery, indicating that all parties would benefit by having the analysis sooner, rather than waiting for the next plan case:

The Commission should find that adherence to a GCR plan, even one approved by the Commission, is not a satisfactory or sufficient explanation for incurring even \$100 million of extra costs. It should direct

⁶² See 2 Tr 80.

MichCon to respond to this concern in any future GCR reconciliation when adherence to its GCR plan caused it to incur extra costs that could have been avoided using a different strategy for acquiring its gas supplies. In any such case, MichCon should be required to present a detailed analysis of what aspect of its GCR plan caused it to incur the extra costs, and how the plan could be modified to avoid those cost in future years.⁶³

Mich Con rejects the Attorney General's contention that the difference between its contract costs and the market value of the gas at the time of delivery should be a source of concern, contending that the \$460 million difference is the expected result of advanced purchases in a declining market. Mr. Clinton testified:

Differing purchasing strategies will produce different financial results in each unique market price environment. The strategy that the Company employed for gas delivered during this GCR period is analogous to a three to five year pricing average. Conversely, buying all gas at index produces a weighted one year price average. It is a mathematical fact that a one year average will yield a lower cost than a longer term average during a falling price environment, which is what has occurred recently. It is also a mathematical fact that a longer term average will out-perform a short term average in a rising price environment. Since the Company cannot know what market environment will occur in any future period, it designs its FPP to perform over the long-term. The fact that a short run approach may have resulted in superior results in any one year provides no constructive insight in designing a FPP for future use.⁶⁴

Mich Con also responds that such an analysis is unnecessary because the company has a different program in place following its 2011-2012 plan case.⁶⁵

This PFD, consistent with the discussion above, acknowledges the importance of the type of evaluation called for by the Attorney General. Nonetheless, since the company's gas supply plan has changed, it is appropriate that any analysis of its actions under the new plan be tailored to the specifics of that plan. It is not feasible in this GCR

⁶³ See 2 Tr 81.

⁶⁴ See 2 Tr 170-171.

⁶⁵ See Clinton, 2 Tr 171-172.

reconciliation to determine the nature of evaluations that should be provided in future reconciliations regarding decisions made under other plans.

As to whether an analysis of the strategies contained in the fixed price purchase guidelines applicable to this GCR period, and the company's implementation of those guidelines, would aid in the development of future plans, this PFD lacks the necessary information to make a recommendation. This PFD notes that in future plan proceedings, the company bears the burden to establish that its plan is reasonable and prudent, and the parties have the opportunity to obtain information, formulate analyses, and cross-examine company witnesses to ensure the company has carefully considered the benefits and potential risks associated with any particular strategy. The company's past experiences, and its understanding of those experiences, may be pertinent.

IV.

MGAT PURCHASES

The MGAT gathering system is connected to Mich Con's transmission and distribution system, and Mich Con records the monthly imbalances attributable to MGAT gas as "exchange gas". The \$1.048 billion cost of purchased gas Mich Con reports in Exhibit A-18 includes 896,929 Mcf of net "exchange gas" delivered to Mich Con by its affiliate MGAT, priced at the "jurisdictional rate" of \$7.9392 per Mcf for a total cost of \$7,120,899.⁶⁶ These volumes are also included in the monthly exchange volumes shown on Ms. Goodwin's Exhibit A-15, line 10. The "jurisdictional rate" is essentially the average cost of gas intentionally purchased for Mich Con's system, including

⁶⁶ See Schmidt, 2 Tr 60-61.

transportation costs.⁶⁷ The Attorney General and the MCAAA both assert that the MGAT imbalance volumes identified in the company's reconciliation should be priced at the Mich Con city-gate index price, rather than the "jurisdictional" rate used by Mich Con.

In Case No. U-16146, Mich Con's GCR plan case for the GCR year ending March 31, 2011, the Commission addressed the treatment of the MGAT balance amounts in its September 28, 2010 order:

[T]he Commission agrees with the ALJ that Mich Con shall prospectively price its MGAT purchases using its monthly city-gate index price rather than the jurisdictional rate. By "prospective," the Commission means all purchases occurring after the Commission issues its final order in this case. In the case where the gas was delivered before the Commission issues this order, but the costs are not approved until after the order, then Mich Con shall book the costs at the city-gate monthly index price.⁶⁸

In Case No. U-15451-R, the reconciliation of Mich Con's gas purchases for the GCR year ending March 31, 2009, the Commission again addressed the question of how these imbalance volumes should be treated. In its October 14, 2010 order, the Commission held:

The Commission agrees with the ALJ and the Staff that the city-gate index price is the appropriate price for MGAT supply on a going forward basis. The Commission further agrees with the ALJ and the Staff in that the city-gate index price applies to purchases delivered before the Commission approves costs in the final order of this case. *Thus, the Commission finds that Mich Con must book the costs at the city-gate monthly price index price for all affiliate purchases going forward from this order.* This includes gas that was received but has not yet been assigned a price prior to the issuance of this order.⁶⁹

⁶⁷ Ms. Schmidt explained that the jurisdictional rate is also used to price gas for company use, lost and unaccounted for gas, and gas in kind. See 2 Tr 62-63.

⁶⁸ September 28, 2010 order, pages 23-24.

⁶⁹ October 14, 2010 order, page 11.

The order further directed, in ordering paragraph C:

Michigan Consolidated Gas Company shall apply the city-gate index price to all future Mich Con Gathering Company supply purchases.⁷⁰

Mich Con sought clarification of the reference at page 11 of this order to “all affiliate purchases “ as quoted above, suggesting that the Commission only meant to address the MGAT imbalance purchases as provided for in the ordering paragraph. The Commission provided the requested clarification in its February 22, 2011 order, stating:

*The Commission finds that the text of the order, on page 11, should be corrected to state that Mich Con must book the costs at the city-gate monthly index price for all MGAT purchases going forward, rather than for all affiliate purchases.*⁷¹

Clearly, then, the Commission intended that the more-appropriate city-gate price be used prospectively for all Mich Con “purchases” of MGAT imbalance volumes after the September 28, 2010 and/or October 14, 2010 orders cited above. But the parties do not agree whether the imbalance volumes at issue in this case should be considered “purchased” prior to that date.

Mich Con now contends that the February 22, 2011 order permits it to continue to use the jurisdictional rate in this reconciliation.⁷² Mich Con cites the rebuttal testimony of Ms. Schmidt, as follows:

MichCon’s treatment of the MGAT costs included in this reconciliation is consistent with the Commission’s order in Case Nos. U-15451-R and U-16146. MichCon has priced its MGAT volumes at the Jurisdictional rate. This purchase was made prior to the Commission’s orders and would not have been a “prospective” purchase at the time of these orders.⁷³

⁷⁰ October 14, 2010 order, page 12,

⁷¹ February 22, 2011 order, page 3.

⁷² See Mich Con’s initial brief, pages 19-21.

⁷³ 2 Tr 68-69.

But Mich Con does not explain or even address the direct testimony of Mr. Clinton, clearly indicating that the gas volumes would not be “purchased” until the Commission issued its decision in Case No. U-15451-R:

Q. Did MichCon purchase imbalance volumes from MichCon Gathering Company (MGAT) during April 2009 through March 2010?

A. No. MGAT imbalances were recorded as exchange gas and appropriately included in the cost of gas as done for all exchange gas accounting. However, *the volumes have not been booked as a purchase at this time*. This is due to the fact that the purchase price for the MGAT imbalance volumes is uncertain and will be determined in the Commission’s Order in Case No. U-15451-R. Once the Commission issues its order in that case, it is MichCon’s intent to book these exchanges with MGAT as purchased gas in the manner approved by the Commission in the Case No. U-15451-R Order.⁷⁴

Ms. Goodwin also testified to the same effect in her direct testimony: “As discussed by Witness Clinton, the MGAT imbalance volumes for the April 2009 - March 2010 period have not been purchased at this time.”⁷⁵ Although the Attorney General cited Mr. Clinton’s testimony in his initial brief, Mich Con did not address this testimony in its reply brief, but merely repeated its initial brief.

This PFD finds that Mich Con did not “purchase” the volumes within the meaning of the Commission’s orders in Case Nos. U-16146 and U-15451-R, but instead deferred the “purchase” of those volumes pending the Commission’s decisions in those cases. Thus, an adjustment to the prices included in the reconciliation for those volumes is appropriate.

⁷⁴ See 2 Tr 137-138.

⁷⁵ See 2 Tr 50.

Mr. Miller and Mr. Peloquin each presented slightly different calculations. Both witnesses used the Mich Con city-gate index prices presented in Exhibit A-1. Mr. Miller added the step of converting the per-Dth city-gate prices to per-Mcf prices using an average Btu conversion factor of 1.0150 Dth per Mcf for all months of the year. His calculations are presented in Exhibit AG-6. Mr. Miller further recommended that the Commission direct Mich Con to perform the exact calculation, using the actual monthly Btu content to convert the volumes of delivered gas measured in Mcfs to Dths. Mich Con, however, did not challenge Mr. Miller's calculation. His testimony indicates that the expected margin of error is relatively small, "perhaps several tens of thousands of dollars".⁷⁶ Therefore, this PFD recommends that the Commission adopt Mr. Miller's recommended disallowance of \$3.3 million.

Note that neither the Attorney General nor MCAAA addressed the calculation of interest on the disallowance. Should the Commission determine that interest is appropriate, the monthly volumes and prices in Exhibit AG-6 should permit the monthly disallowance amounts to be calculated; from those monthly amounts, the monthly columns in Exhibits A-18 and A-21 can be adjusted, and interest determined accordingly.

V.

AFFILIATE TRANSACTIONS

Focusing heavily on Mich Con's dealings with MGAT as discussed above, and also noting that Mich Con purchased approximately .5 Bcf of gas from its affiliate DTE

⁷⁶ See 2 Tr 88.

Energy Trading, the MCAAA urges the Commission to take additional measures to address affiliate transactions comprehensively for the utility. Mr. Peloquin testified:

As can be seen, as a holding company, DTE [Energy Company] owns MichCon, Detroit Edison, and a number of unregulated subsidiaries or affiliates, all heavily engaged in the energy business. This structure establishes the opportunity and incentive for the various utility subsidiaries, and the other affiliates, to self-deal within the holding corporate structure to benefit the holding Company, either directly or indirectly, and to the actual or potential detriment of ratepayers of the regulatory utility.

The potential for abuse is heightened to the degree that MichCon and the parent company, DTE, have interlocking top management, or combined “service company entities.” MichCon has presented no evidence that there exists checks and balances, or some independent top management at MichCon, to protect MichCon (and its ratepayers) in the event of conflicts with its parent company, DTE Energy, or its sister DTE subsidiary, Detroit Edison; or affiliates thereof, and also with other non-regulated affiliates.⁷⁷

Although he presented as exhibits numerous discussions of a regulatory concept known as “ring fencing”, his recommendations in this case were limited to the following, with the numbering added for ease of discussion:

[1] The Commission should require MichCon to file in GCR plan and reconciliation cases complete evidence describing in detail all of its transactions with affiliates of MichCon, DTE, Detroit Edison, and their affiliates (i.e. all affiliates) and establishing that such transactions were or are reasonable and prudent, and consistent with MichCon’s duty to minimize the cost of gas.

[2] The Commission should establish a process, and assign resources thereto, to obtain the books and records of the utility, and of all affiliates, and to review and audit same, as necessary to ensure that MichCon (and its ratepayers) are not cross-subsidizing affiliates. However, I am limiting my recommendation in this proceeding. I am specifically requesting the Commission to open up the books and records of MGAT in all future GCR Reconciliation cases.

⁷⁷ See 2 Tr 101-102.

[3] The Commission should require MichCon to file an annual report describing all efforts and protective measures MichCon has in place or is undertaking to ensure that MichCon is not cross-subsidizing its parent company, or its affiliates, or MichCon's own affiliates (all affiliates), and to ensure that the utility is protected from adverse impacts affecting said affiliates arising from past, present, or future obligations or dealings.⁷⁸

The MCAAA's briefs quote at length from Mr. Peloquin's testimony and generally ask that the Commission adopt his recommendations.

MichCon addressed Mr. Peloquin's recommendations in both its initial brief and in its reply brief. Treating the MCAAA's recommendations as a recommendation that the Commission "adopt the concept of 'ring fencing'",⁷⁹ Mich Con argues that the MCAAA's recommendations are irrelevant and are outside the proper scope of an Act 304 proceeding:

The concept of "ring fencing" is not an issue related to expenses for gas supply for 2009-2010 GCR year. Accordingly, Witness Peloquin's recommendations that the Commission adopt the undefined concept of "ring fencing" and require MichCon to file an annual report regarding affiliate companies are not relevant to this GCR reconciliation proceeding because such recommendations are of no consequence to the determination of the only statutorily permissible issue for this GCR reconciliation proceeding, which is limited by the unambiguous statutory language of Act 304 to the reconciliation of expenses incurred by MichCon for gas costs for the 2009-2010 GCR Year.⁸⁰

Mich Con renews objections to consideration of the MCAAA's Exhibits MCAAA-2 through MCAAA-4 as irrelevant and as hearsay. In its reply brief, Mich Con further argues that by raising the issue of "ring fencing" in Detroit Edison's recent rate case, the MCAAA implicitly acknowledged that a GCR reconciliation is not the place to consider

⁷⁸ See 2 Tr 104.

⁷⁹ See Mich Con brief at 17.

⁸⁰ Mich Con initial brief, pages 18-19.

such issues.⁸¹ And in its reply brief and a separately filed motion, Mich Con asks that a portion of the MCAAA's brief be struck because it quotes from an article that is not part of the evidentiary record in this proceeding.

First, this PFD finds that Mich Con's jurisdictional arguments are not well taken. The MCAAA's requests are addressed to the Commission's discretion. There can be no doubt that the Commission has discretion to require the utility to submit information on its transactions with affiliates, in this proceeding, or on its own, and the Commission can look to the record in any case to inform its discretion.⁸² Moreover, while Mich Con focuses on Act 304 as encompassing "questions of reasonableness and prudence that could not have been adequately addressed in the plan case," Mich Con does not dispute Mr. Miller's assertion that the MGAT transactions were not part of the company's plan case filing. Clearly, where the Commission is confronted in a reconciliation with an issue that was not presented in a plan case, the Commission may want to take remedial measures to prevent that from happening again, and nothing in Act 304 precludes such measures.

This PFD notes that the Commission has long been concerned with affiliate transactions engaged in by regulated utilities and taken numerous steps to protect ratepayers. For example, in Case Nos. U-10149 and U-10150, the Commission adopted conditions regarding affiliate transactions designed to ensure it could effectively safeguard the public interest.⁸³ Subsequently, in Case No. U-13502, Detroit Edison Company agreed to adopt the same affiliate transaction conditions.⁸⁴ In

⁸¹ Mich Con reply brief, pages 3-7.

⁸² See MCL 460.55.

⁸³ See October 28, 1993 order, pages 125-129.

⁸⁴ See January 21, 2003 order.

Case No. U-11145, the Commission reiterated that transactions between Mich Con and its affiliate MCN Investment Corp. for the acquisition of GCR system supply were subject to scrutiny for reasonableness and prudence in accordance with Act 304.⁸⁵ Recently, in Case No. U-15451-R, Mich Con's reconciliation for the GCR year prior to the one at issue in the instant case, the Commission expressly acknowledged a concern for affiliate transactions:

[T]he Commission acknowledges the concern regarding affiliate purchases and the lack of evidence justifying the choice of an affiliate over a competitor. Thus, the Commission directs Mich Con to provide the Staff with information regarding the company's selection of an affiliate for each purchase of gas supply.⁸⁶

Nonetheless, on the basis of this record, this PFD does not recommend that the Commission adopt any remedial measures focused on Mich Con's affiliate transactions. With regard to MGAT specifically, the Commission has already addressed the treatment of MGAT transactions in its decisions in Case Nos. U-16146 and U-15451-R. Limiting the costs of affiliate transactions that may be passed through to ratepayers is one of the principal means by which the Commission protects ratepayers from the potential for affiliate abuse.

The first remedial measure identified by Mr. Peloquin, quoted above, seeks to have Mich Con disclose its affiliate transactions and provide support for the reasonableness and prudence of those transactions in plan and reconciliation proceedings. This appears unnecessary because Mich Con is required to support the reasonableness and prudence of all of its transactions in plan and reconciliation proceedings. The MCAAA has not identified any specific information missing from this

⁸⁵ See August 13, 1997 order, page 14.

⁸⁶ See October 14, 2011 order, page 11.

reconciliation. While Mich Con did not contradict Mr. Miller's testimony that the MGAT gas volumes were not included in the company's plan, this omission was addressed in Case No. U-16146. In its September 22, 2011 order in that case, the Commission adopted the Administrative Law Judge's recommendation that in future plan cases, the company should formally acknowledge its reliance on MGAT gas.⁸⁷

The second remedial measure identified by Mr. Peloquin, quoted above, seeks access to the books and records of MGAT in future GCR proceedings. This PFD does not recommend the Commission make any general pronouncements regarding those books and records at this point, since there has been no showing that parties to this proceeding were unable to obtain any relevant evidence regarding Mich Con's dealings with MGAT. Instead, the only issue raised in this proceeding regarding Mich Con's gas supply costs during the GCR year was how to interpret the Commission's orders in Case Nos. U-16146 and U-15451-R and the company's testimony that it had not yet purchased the MGAT volumes. Again, the conditions adopted in the Commission orders cited above make clear that the Commission has access to the books and records of affiliates doing business with the utility.

The third remedial measure identified by Mr. Peloquin, quoted above, calls for an annual report to be filed by Mich Con identifying affiliate transactions and policies and other measures in place to ensure no cross-subsidization or other adverse impacts to the utility. The Commission already has annual reporting requirement for utilities, and the MCAAA does not explain how its proposed requirement would overlap with existing

⁸⁷ Note that in its June 12, 1992 order in Case No. U-9902, the Commission admonished Mich Con to include information on all anticipated supply sources in its plan case five-year forecast.

requirements. This PFD declines to recommend, on the basis of this record, that the Commission require additional annual reporting by the utilities.

Finally, it is necessary to address the motion to strike a portion of the MCAAA's brief relating to the issue of affiliate transactions. Mich Con's motion seeks to strike the portion of the MCAAA brief that references and quotes from a journal article entitled "Repeal of the Public Utility Holding Company Act of 1935. Implications and Options for State Commissions," by Robert E. Burns and Michael Murphy, *Electricity Journal*, Volume 19, Issue 8, October 2001. Mich Con argues that this document was never made part of the evidentiary record in this proceeding and is therefore inadmissible for consideration by the ALJ and the Commission pursuant to Rule 325 of the Commission's Rules of Practice and Procedure, the Michigan Rules of Evidence, and the Michigan Constitution. Characterizing the article as hearsay, Mich Con asserts that the MCAAA's counsel "is essentially testifying as an expert witness", and contends that consideration of the article will deny Mich Con its due process rights, the "fair and just treatment" guaranteed by the Michigan Constitution, and the opportunity to submit opposing evidence and dispute the context, admissibility and relevance of the article.

The MCAAA responds that the disputed article is a legal treatise concerning aspects of the 2005 Energy Policy Act, and its implications for state regulation, and as such it is wholly appropriate for inclusion in the MCAAA's legal brief. The MCAAA asserts that the article deals with legal matters, rather than facts or documentary evidence, and as such, is not required to be placed into an evidentiary record. The MCAAA further disputes any prejudice to Mich Con, contending that the article is readily available on the internet and by means of other legal research services.

While noting that this PFD has not relied on this article in formulating recommendations to the Commission, for the reasons stated prior to the discussion of this motion, this PFD declines to grant Mich Con's motion. The article cited by the MCAAA is in the nature of a legal treatise, and was not discussed in MCAAA's brief to establish any fact in dispute, but to further the legal and policy positions of the MCAAA that affiliate transactions are a matter of general concern and that the Commission has authority to protect ratepayers from potential abuse.

VI.

CONCLUSION

All contentions of the parties not specifically addressed and determined herein are rejected, the Administrative Law Judge having given full consideration to all evidence of record and arguments in arriving at the findings and conclusions set forth in this Proposal for Decision. Based on the foregoing discussion and findings, this PFD recommends that the Commission find the following:

1. Mich Con operated its system in a reasonable and prudent manner during the GCR year under review;
2. Mich Con failed to show its gas purchasing practices were reasonable and prudent, but no party proposed a disallowance related to that failure that was supported on this record;
3. Mich Con should be cautioned as recommended above regarding its purchasing practices and its documentation of those practices;

4. MGAT imbalance volumes should be priced at the Mich Con city-gate monthly index price, resulting in a disallowance of \$3.3 million, and a total overrecovery for the GCR period of \$6.2 million before interest is applied; and

5. Mich Con's reconciliation should otherwise be accepted.

MICHIGAN ADMINISTRATIVE HEARING
SYSTEM
For the Michigan Public Service Commission

Sharon L. Feldman
Administrative Law Judge

July 14, 2011
Lansing, Michigan
drr